

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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OFFICE OF THE SECRETARY

In the Matter of)	
)	
1998 Biennial Regulatory Review –)	
Review of Depreciation Requirements)	CC Docket No. 98-137
for Incumbent Local Exchange Carriers)	
)	
Ameritech Corporation Telephone Operating)	
Companies' Continuing Property Records)	CC Docket No. 99-117
Audit, et. al.)	
)	
GTE Telephone Operating Companies)	
Release of Information Obtained During)	AAD File No. 98-26
Joint Audit)	

ERRATUM TO
COMMENTS OF U S WEST COMMUNICATIONS, INC.

Please substitute the attached Comments of U S WEST Communications, Inc. originally filed April 17, 2000. This erratum corrects a typographical error in the first line of the first full paragraph on page 2 changing "depreciation proposed" to "depreciation proposal." Also, due to a technical error which occurred during the conversion from a Word document to a PDF document (for electronic submission), portions of the text in footnotes 17 and 21 were omitted. This erratum corrects those footnotes as well.

U S WEST apologizes for any inconvenience this may cause.

Respectfully submitted,

U S WEST COMMUNICATIONS, INC.

By: James T. Hannon
James T. Hannon
Suite 700
1020 19th Street, N.W.
Washington, DC 20036
(303) 672-2860

Its Attorney

Of Counsel,
Dan L. Poole

April 20, 2000

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COMMENTS OF U S WEST COMMUNICATIONS, INC.

The Federal Communications Commission (“Commission”) initiated this Further Notice of Proposed Rulemaking (“Notice” or “FNPRM”) ¹ in response to an Ex Parte filed by the Coalition for Affordable Local and Long Distance Service (“CALLS Coalition”) on March 3, 2000.² In their Ex Parte the CALLS Coalition members laid out a process “to eliminate the disparity that exists between the regulatory and financial accounting for depreciation expense

¹ In the Matter of 1998 Biennial Regulatory Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers, Ameritech Corporation Telephone Operating Companies’ Continuing Property Records Audit, et. al., GTE Telephone Operating Companies Release of Information Obtained During Joint Audit, CC Docket No. 98-137, CC Docket No. 99-117, AAD File No. 98-26, Further Notice of Proposed Rulemaking, FCC 00-119, rel. Apr. 3, 2000.

² See Ex Parte letter to Mr. Lawrence Strickling, Chief, Common Carrier Bureau from Frank J. Gumper, Bell Atlantic Network Service, Robert Blau, BellSouth Corporation, Donald E. Cain, SBC Telecommunications, Inc. and Alan F. Ciamporzero, GTE Service Corporation in CC Docket Nos. 96-262, 94-1, 99-249 and 96-45, dated March 3, 2000 (“March 3 Ex Parte letter”).

and associated reserve balances.”³ They proposed to achieve this by filing a joint petition for waiver in accordance with the Commission’s recent Depreciation Order.⁴

While the CALLS Coalition’s depreciation proposal varies somewhat from the waiver conditions outlined in the Depreciation Order,⁵ it addresses the concerns which the Commission raised in denying the United States Telephone Association’s (“USTA” n/k/a United States Telecom Association) petition for forbearance and in its biennial review of depreciation. The current FNPRM notes that the waiver process contemplates a case-by-case review and that it might be more appropriate to modify the Commission’s rules for all price cap carriers.⁶ As such, the Commission requests comments on the CALLS depreciation proposal and its potential impact.

I. INTRODUCTION AND SUMMARY

As a price cap carrier and non-signatory to the CALLS proposal U S WEST Communications, Inc. (“U S WEST”) has a significant interest in the outcome of any Commission rule change that affects depreciation rates for price cap local exchange carriers

³ Id. at 1.

⁴ In the Matter of 1998 Biennial Regulatory Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers, United States Telephone Association’s Petition for Forbearance from Depreciation Regulation of Price Cap Local Exchange Carriers, Report and Order in CC Docket No. 98-137, Memorandum Opinion and Order in ASD 98-91, 15 FCC Rcd. 242, 247-49 ¶¶ 11-17 (1999) (“Depreciation Order”).

⁵ “Specifically, we find that such a waiver may be approved when an incumbent LEC, voluntarily, in conjunction with its request for waiver: (1) adjusts the net book costs on its regulatory books to the level currently reflected in its financial books by a below-the-line write-off; (2) uses the same depreciation factors and rates for both regulatory and financial accounting purposes; (3) foregoes the opportunity to seek recovery of the write-off through a low-end adjustment, an exogenous adjustment, or an above-cap filing; and (4) agrees to submit information concerning its depreciation accounts, including forecast additions and retirements for major network accounts and replacement plans for digital central offices.” Id. at 252-53 ¶ 25 (footnotes omitted).

⁶ Id. at 244 ¶ 3.

("LEC"). U S WEST is not opposed to eliminating depreciation requirements for price cap carriers and has supported the elimination of these requirements on numerous occasions.⁷ However, this support does not translate into support for the CALLS Coalition's depreciation proposal contained in their Ex Parte or the waiver conditions that the Commission articulated in its Depreciation Order.

While the incumbent LECs signing the Ex Parte may "voluntarily" choose to accept conditions that can only be described as unreasonable, for the right to use the same depreciation rates for regulatory purposes as for financial reporting purposes -- U S WEST does not care to join in this act of self-sacrifice.⁸ This proposal unfairly harms shareholders' interests. Any possibility that shareholders might be able to recover the costs of their investments would be eliminated under this plan. This harm to shareholders is real and cannot be ignored, particularly after ratepayers have benefited from decades of unrealistically low depreciation rates. Despite the repetitious comments in both the Depreciation Order and FNPRM about potential harm to consumers -- there can be none as long as carriers do not recover more through depreciation rates than they have invested.⁹ These claims of concern about potential harm to consumers are a slim

⁷ See, e.g., Reply of U S WEST, CC Docket No. 92-296, filed Mar. 10, 1993, Comments of U S WEST Communications, Inc., CC Docket No. 92-296, filed Dec. 17, 1993, Comments of U S WEST, CC Docket No. 92-296, filed Nov. 14, 1994, U S WEST Petition for Reconsideration, CC Docket No. 92-296, filed Dec. 6, 1993 and Comments of U S WEST, Inc., CC Docket No. 98-137 and ASD 98-91, filed Nov. 23, 1998.

⁸ Even if U S WEST supported the CALLS price cap proposal, it would not voluntarily accept the conditions for elimination of depreciation regulation which were articulated in the CALLS Coalition's March 3, 2000 Ex Parte.

⁹ The suggestion that consumers will be harmed by adopting more realistic service lives for telephone plant is totally at odds with the fundamental premises underlying the last century of public utility ratemaking. If there is any "harm" to current ratepayers, it is the result of past depreciation policies which must now be corrected.

justification for continued regulation of depreciation rates in one form or another, long after such regulation has served any useful purpose.

Both the Depreciation Order and Notice demonstrate that the Commission just “can’t let go” when it comes to the regulation of depreciation rates for price cap LECs.¹⁰ Clearly, after years of experience with price cap regulation and the subsequent elimination of sharing there is no need or justifiable reason for the continued regulation, let alone micromanagement, of depreciation rates for price cap companies. Furthermore, Sections 10 and 220 of the 1996 Act removed any legal impediment that may have previously prevented the Commission from eliminating depreciation regulation for price cap companies.¹¹

It is unfortunate that the price for elimination of the Commission’s depreciation rules is the requirement that price cap LECs “voluntarily” relinquish their rights to recover existing depreciation reserve deficiencies.¹² Furthermore, it is troubling that the Commission could adopt rules in this proceeding which would turn these voluntary commitments into mandatory requirements for all price cap LECs.¹³ Such an approach is ill-advised and would immediately raise the issue of whether LEC property has been taken without either specific authority or just compensation.

¹⁰ See generally, Letting Go: Deregulating the Process of Deregulation, by Alfred E. Kahn, 1998, Michigan State University, Institute of Public Utilities and Network Industries.

¹¹ Prior to the 1996 Act, it could be argued that the Commission was required to regulate depreciation rates and practices of LECs by Section 220(b). This justification no longer exists with the Act’s revision of Section 220(b) and the addition of Section 10 which gives the Commission the authority to forbear from regulation.

¹² It is ironic in referring to the public interest, never once does the Commission mention investors and the fact that the public interest is ill-served if LECs are prohibited from recovering invested capital through reasonable and economic depreciation rates.

¹³ FNPRM ¶ 3.

In addition to U S WEST's fundamental disagreement with the Commission's Depreciation Order and the direction the FNPRM appears to be headed, the relief that the Notice offers appears to be more illusory than real.¹⁴ This is unfortunate given the high price that the Commission has established for relief from depreciation regulation. In the sections which follow, U S WEST addresses the specifics of the Commission's FNPRM, despite U S WEST's fundamental disagreement with the Commission's approach to depreciation regulation for price cap carriers.

II. THE COMMISSION DOES NOT HAVE THE AUTHORITY TO
ADOPT OR ENFORCE ANY RULES, COMMITMENTS OR
VOLUNTARY AGREEMENTS REGARDING STATE DEPRECIATION
RATES OR PRACTICES

Regardless of whether there is any need to be concerned about the States¹⁵ -- and U S WEST does not believe there is -- the Commission has no jurisdiction to establish depreciation rates or practices at the State level. The Supreme Court was explicitly clear in

¹⁴ Even if the Commission approved the CALLS depreciation proposal in one form or another, LECs would continue to be subject to at least the same amount of record keeping as is currently required with separate depreciation rates for regulatory and financial purposes. With this Notice, it appears that the Commission is proposing to increase the record-keeping burden rather than decrease it.

¹⁵ In CC Docket No. 98-137, U S WEST pointed out that the fourteen States which it served -- many of which are small and rural -- all established depreciation service lives that are different from those prescribed by the Commission. In every case these States had at least one depreciable life below the Commission's prescribed ranges. See Comments of U S WEST, Inc., CC Docket No. 98-137, filed Nov. 23, 1998 at 9, Reply Comments of U S WEST, Inc., CC Docket No. 98-137, filed Dec. 8, 1998 at 3.

Louisiana Public Service that under Section 2(b) of the Act,¹⁶ States retain jurisdiction over depreciation charges and practices for intrastate telephone plant.¹⁷

The Commission should not be concerned about adverse impacts at the State level. The States are fully capable of making their own decisions with respect to depreciation, as the Commission is well aware from earlier three-way meetings.¹⁸ As such, the Commission should limit the current proceeding to interstate matters. Any attempt to condition interstate relief on “firm commitments” at the State level¹⁹ would be both ill-advised and unlawful.²⁰ U S WEST

¹⁶ Section 2(b) of the Act provides that “nothing in this chapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier, . . .” 47 U.S.C. § 152(b).

¹⁷ Louisiana Public Service Commission v. FCC, 476 U.S. 355, 374 (1986). “Section 152(b) constitutes, . . . a congressional *denial* of power to the FCC to require state commissions to follow FCC depreciation practices for intrastate ratemaking purposes,” and at 356, “The FCC may not take ‘preemptive’ action merely because it thinks such action will best effectuate federal policy.”

¹⁸ See, e.g., In the Matter of The Prescription of Revised Percentages of Depreciation pursuant to the Communications Act of 1934, as amended for: The Bell Telephone Company of Pennsylvania, BellSouth Telecommunications, Inc., The Chesapeake and Potomac Telephone Company, The Chesapeake and Potomac Telephone Company of Maryland, GTE Florida Incorporated, GTE Hawaiian Telephone Company, Incorporated, Indiana Bell Telephone Company, Incorporated, Michigan Bell Telephone Company, New York Telephone Company, Southwestern Bell Telephone Company, U S West Communications, Inc., United Telephone-Southeast, Inc., Wisconsin Bell, Inc., Memorandum Opinion and Order, 8 FCC Rcd. 816 (1993); and see 47 U.S.C. § 220(i).

¹⁹ See Notice n.25 and ¶¶ 12-13. Any such action would unlawfully involve the Commission in intrastate ratemaking in violation of Section 2(b) of the Act. See Texas Office of Pub. Util. Counsel v. FCC, 183 F.3d 393 (5th Cir. 1999), pets. for reh’g and reh’g denied, where the Court found that the Commission’s requirement that both intra- and interstate revenues be included in calculating carrier universal service fund contributions to be a violation of Section 2(b).

²⁰ See, e.g., NARUC v. FCC, 880 F.2d 422, 428-30 (D.C. Cir. 1989), wherein the Court granted the petition for review on the grounds that Commission deregulatory action in the federal jurisdiction regarding the installation and maintenance of simple inside wiring was not necessarily a condition that triggered preemption of state regulation in this area.

fully intends to seek recovery of all expenses lawfully incurred in the provision of intrastate service, including depreciation expense and any applicable depreciation reserve deficiency.

III. ANY AMORTIZATION OF THE DEPRECIATION RESERVE DEFICIENCY SHOULD BE ABOVE-THE-LINE

It would be unwise and unlawful for the Commission to require a below-the-line amortization of the depreciation reserve deficiency.²¹ This deficiency exists solely because regulated depreciation rates have not properly reflected the true economic lives of telephone plant.²² There is no justification for suggesting that LECs forego recovering this expense long

²¹ It has long been good law that expenses, such as depreciation, associated with prudent investments are allowable in utility ratemaking. See West Ohio Gas Co. v. Public Utilities Commission of Ohio, 294 U.S. 63, 72 (1934). Above-the-line accounting creates a presumption that such expenses will be included in a carrier's revenue requirement for ratemaking purposes. In fact, Courts have found litigation expenses arising out of a utility's core business to be properly accounted for above-the-line. See Appalachian Electric Power v. FPC, 218 F.2d 773, 777 (4th Cir. 1955) "[T]here is no reason why the cost of such [litigation] proceedings should not be treated as a part of the cost of the property to which they related. . . . The litigation was unquestionably undertaken for the benefit of the project which was ultimately licensed, and the costs of that litigation were a part of the legitimate costs of bringing that project into being" "and thus for the benefit of ratepayers." Also see, Mountain. States Telephone and Telegraph Company et al. v. FCC, 939 F.2d 1035, 1043 (D.C. Cir. 1991).

²² In the past, U S WEST has had little success in its numerous requests for shorter, more realistic depreciation lives. These efforts have been discontinued in recent years as it has become increasingly obvious that the Commission is unwilling to consider the speed of technological change in the telecommunications industry in establishing depreciation lives. Despite claims that it is prescribing forward-looking rates, the Commission continues to focus on historical retirement rates (as reported in ARMIS) and declines to consider forecasts of future service lives such as those provided by Technological Futures, Inc. ("TFI") in CC Docket No. 98-137. This is demonstrated by the Commission's recent Depreciation Order where the Commission stated "[I]f the carriers do begin to retire plant more rapidly, our depreciation prescription process is flexible enough to allow them shorter lives and faster depreciation.[footnote omitted] We conclude, therefore, that the TFI study fails to establish convincingly that current projection lives are inadequate." Depreciation Order, 15 FCC Rcd. at 249 ¶ 16. What TFI failed to show was that its view of future service lives agreed with historical retirements. Such an approach ensures that large incumbent LECs, the only group of telecommunications carriers still subject to the Commission's pervasive depreciation rules, will never "catch-up" in a fast-changing, highly-competitive telecommunications environment where product lives have gotten shorter and shorter. Thus, despite the "lack of certainty" with future forecasts of service lives, this is exactly

after capital has been invested to provide interstate service. As such, if an amortization is allowed, it should be above-the-line and expenses and benefits²³ associated with it should be reflected in all rate of return calculations that LECs are required to provide under price cap regulation.

This in no way implies that interstate rates are expected to increase under price cap regulation, as a result of amortizing the depreciation reserve deficiency. This is unlikely. However, amortization expenses should be treated like any other lawful expenditure. If a combination of revenue shortfalls and other expenses push LEC earnings below the low-end adjustment, price cap LECs should be allowed to reflect this adjustment in the next annual tariff filing. This is far different from an exogenous adjustment which would immediately increase rates over the life of the amortization.²⁴

IV. IF THE COMMISSION ADOPTS RULES SIMILAR TO THOSE PROPOSED BY THE CALLS COALITION, COMPLIANCE SHOULD BE DISCRETIONARY RATHER THAN MANDATORY

The CALLS Ex Parte, which stimulated the Commission to issue the instant FNPRM, addressed the waiver requirements contained in the Commission's Depreciation Order.²⁵ There was no hint that all price cap LECs might be subject to these same conditions until the release of the FNPRM. U S WEST understands that it may serve the interests of administrative efficiency

the direction that the Commission must move if it wants to ensure that there is a strong and financially viable public switched network.

²³ Such as unamortized investment tax credits and excess deferred taxes.

²⁴ While original price cap rates may have been set too low due to inadequate depreciation rates, U S WEST is neither requesting nor suggesting that amortization costs be reflected in an exogenous adjustment. However, under existing price cap rules it would be inequitable and unprecedented to disallow a certain category of expenses for purposes of determining whether the low-end adjustment is triggered.

²⁵ Depreciation Order, 15 FCC Rcd. at 252-53 ¶ 25.

to promulgate a single set of rules for price cap companies requesting similar relief rather than processing individual waiver requests. However, if the Commission determines that it is appropriate to adopt rules after consideration of the comments filed in this proceeding, all price cap carriers should be given the option to voluntarily operate under such rules. A mandatory requirement could be unlawful in that it would preclude price cap LECs from any opportunity of recovering prudently-invested capital during the proposed five-year amortization period through any lawful means.²⁶

V. THE FACT THAT AN AMORTIZATION MAY MOOT ANY CONCERNS WITH CPR AUDITS IN NO WAY IMPLIES THAT THE ASD'S "FINDINGS" ARE NOT FATAL FLAWED

The Commission has taken no position on the Accounting Safeguards Division's ("ASD") draft Continuing Property Records ("CPR") audit findings.²⁷ Furthermore, U S WEST has presented extensive evidence showing that the ASD's audit is fatally flawed both in terms of its sample results and the statistical methodology that the ASD employed in extrapolating sample results to U S WEST's overall investment in hardwired COE equipment.²⁸ Even Commissioner

²⁶ Bluefield Water Works & Improvement Company v. Public Service Commission of the State of West Virginia, et al., 262 U.S. 679, 692 (1923) "A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties." Also see Duquesne Light Co. v. Barasch, 488 U.S. 299 (1988); FPC v. Hope Natural Gas Co., 320 U.S. 591 (1944).

²⁷ In issuing its Notice of Inquiry on the CPR audits conducted by the ASD, "[T]he Commission stated that it was not passing judgment on the accuracy of the [audit] reports, their findings or conclusions." In the Matters of: Ameritech Corporation Telephone Operating Companies' Continuing Property Records Audit, etc., Notice of Inquiry, 14 FCC Rcd. 7019 ¶ 1 (1999). In commenting on the ASD's Public Notice concerning its rescoring methodology, the Commission stated: "As with the audit reports themselves, the Commission does not pass judgment on the accuracy or merit of the procedures described in the ASD Public Notice. Id. at 7021 n.2.

²⁸ See Comments of U S WEST, CC Docket No. 99-117, filed Sep. 23, 1999 and Reply Comments of U S WEST, CC Docket No. 99-117, filed Oct. 25, 1999.

Furchtgott-Roth questioned the validity of the ASD's methodology and audit findings.²⁹ Thus, U S WEST believes that the CPR audits are irreparably flawed and should be terminated -- and has requested that they be on numerous occasions. The fact that a "non-recoverable amortization" may moot any potential CPR concerns in no way suggests that the audits have any validity themselves.

VI. CONCLUSION

For the foregoing reasons, U S WEST cannot support the CALLS Coalition depreciation proposal. If the Commission does adopt rules implementing this proposal, compliance should be discretionary rather than mandatory.

Respectfully submitted,

U S WEST COMMUNICATIONS, INC.

By: James T. Hannon
James T. Hannon
Suite 700
1020 19th Street, N.W.
Washington, DC 20036
(303) 672-2860

Its Attorney

Of Counsel,
Dan L. Poole

April 17, 2000

²⁹ See Separate Statement of Commissioner Harold Furchtgott-Roth Dissenting in Part in In the Matter of US West Telephone Operating Companies' Continuing Property Records Audit, Order, 14 FCC Rcd. 5731, 5828-36 (1999).

CERTIFICATE OF SERVICE

I, Kristi Jones, do hereby certify that I have caused 1) the foregoing **ERRATUM TO COMMENTS OF U S WEST COMMUNICATIONS, INC.** to be filed electronically with the FCC by using its Electronic Comment Filing System, 2) a courtesy copy of the **ERRATUM** to be served, via hand delivery, upon all persons listed on the attached service list, and 3) a diskette copy of the **ERRATUM** to be served, via hand delivery, upon the International Transcription Services, Inc.

Kristi Jones

Kristi Jones

April 20, 2000

William E. Kennard
Federal Communications Commission
8th Floor
Portals II
445 12th Street, S.W.
Washington, DC 20554

Gloria Tristani
Federal Communications Commission
8th Floor
Portals II
445 12th Street, S.W.
Washington, DC 20554

Michael K. Powell
Federal Communications Commission
8th Floor
Portals II
445 12th Street, S.W.
Washington, DC 20554

Harold Furchtgott-Roth
Federal Communications Commission
8th Floor
Portals II
445 12th Street, S.W.
Washington, DC 20554

Susan P. Ness
Federal Communications Commission
8th Floor
Portals II
445 12th Street, S.W.
Washington, DC 20554

Lawrence E. Strickling
Federal Communications Commission
Room 5-C345
Portals II
445 12th Street, S.W.
Washington, DC 20554

Kenneth P. Moran
Federal Communications Commission
Room 6-B201
Portals II
445 12th Street, S.W.
Washington, DC 20554

Debbie Byrd
Federal Communications Commission
6th Floor
Portals II
445 12th Street, S.W.
Washington, DC 20554

International Transcription
Services, Inc.
1231 20th Street, N.W.
Washington, DC 20036

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